

ST 01-0006-PLR 02/15/2001 MANUFACTURER'S PURCHASE CREDIT

Purchasers of manufacturing machinery and equipment that qualifies for the manufacturing machinery and equipment exemption earn a credit in an amount equal to a fixed percentage of the tax which would have been incurred under the Use Tax or Service Use Tax. See 35 ILCS 105/3-85, 35 ILCS 110/3-70. (This is a PLR.)

February 15, 2001

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see <http://www.revenue.state.il.us/legalinformation/regs/part1200>), is in response to your letter of December 5, 2000. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

On behalf of our client, COMPANY ('Company'), FIRM is requesting a private letter ruling regarding Illinois treatment of sales/use tax law as it relates to the following facts. We have enclosed a copy of form IL-2848, Illinois Power of Attorney, authorizing us to correspond with you regarding this request.

Facts:

The Company manufactures and sells casket hardware as well as performs contract metal fabrication and finishing.

The Company purchases molds and dies that are used in the manufacturing of the above mentioned products. The Company purchases these items tax free pursuant to the Manufacturing Machinery and Equipment exemption.

The molds and dies purchased are made pursuant to the specifications of Company to fulfill orders from its customers. These orders are recurring and not limited to one-time orders.

The Company believes the proper base for the Manufacturer's Purchase Credit ('MPC') is 100% of the purchase price of such molds and dies.

During a recent sales and use tax audit, the Company was limited to 50% of the purchase price of such molds and dies in computing the MPC. The auditor was unable to provide documentation to support her position in limiting the purchase price to 50%. For administrative convenience only, the Company elected to not pursue the issue with the auditor.

Question:

Is the Company's position that the MPC should apply to 100% of the purchase price of the molds and dies used in the manufacturing of products for sale to customers correct?

Discussions:

In determining what percentage Company should be utilizing in earning the MPC, we have referred to the Service Occupation Tax and the Service Use Tax statutes and regulations. According to the Illinois Regulation 86 Illinois Administrative Code 140.201(e)(7), a 'Sale of Service' means any transaction **except** *'a sale or transfer of machinery and equipment used primarily in the process of manufacturing or assembling, either in an existing, an expanded or a new manufacturing facility, of tangible personal property for wholesale or retail sale or lease, whether such sale or lease is made directly by the manufacturer or some other person, whether the materials used in the process are owned by the manufacturer or by some other person, or whether such sale or lease is made apart from or as an incident to the seller's engaging in the service occupation of producing machines, tools, dies, jigs, patterns, gauges or other similar items of no commercial value on special order for a particular purchaser, when the machinery or equipment is produced by the seller thereof for the manufacturer or the manufacturer's lessor on special order in such a way as to have made the applicable tax a Service Occupation Tax or Service Use Tax, rather than Retailer's Occupation Tax or Use Tax.'* The same wording is found in the Illinois Compiled Statutes Service Use Tax Act definitions, 35 ILCS 110 Section 2. From this broad definition, it appears that the molds and dies utilized by Company do not fall into the definition of a 'Sale of Service' and would therefore be subject to any applicable taxes at 100% of the selling price.

Additionally, under the Service Use Tax Act Section 2, 'Selling price' is defined as *'the consideration for a sale valued in money whether received in money or otherwise, including cash credits and service, and shall be determined without any deduction on account of the serviceman's cost of the property sold, the cost of materials use,; labor or service cost or any other expense whatsoever...'* Based upon this definition of selling price, it does not appear that the state can utilize the 50% tax base rule.

In Section 3-10 of the Illinois Compiled Statutes Service Occupation Tax Act, 35 ILCS 115, the statutes imply that a 50% tax base may not be utilized in a situation where a serviceman contracts to design, develop, and produce special order machinery or equipment. The Act specifically states *'...the tax imposed by this Act shall be based on the serviceman's cost price of the tangible personal property transferred incident to the completion of the contract.'*

Finally, Letter Ruling ST 91-0348 dated April 26, 1991 puts forth the question of whether or not a difference exists in the taxability of molds and dies if they are made to order or sold at retail. The State's position in this Letter Ruling was that there is no

difference between the two situations. Carrying forward this same thought pattern to the MPC, it would appear that Company should be able to earn the MPC on 100% of the purchase price regardless of whether the molds and dies are special order or sold to them at retail.

We could not locate contradictory cases or previous letter rulings addressing a similar set of facts as established in this request. To the best of our knowledge, the Illinois Department of Revenue has not previously ruled on the same or similar issue for Company and no previous letter ruling has been requested by Company regarding this issue. There is currently no audit or pending litigation with the Illinois Department of Revenue.

Conclusion:

Based on the above research, it does appear that Company's belief that the proper base for earning the MPC on 100% of the purchase price of their molds and dies used in the manufacturing process is correct.

Thank you in advance for your assistance in this matter. If you have any questions regarding any of the information provided, please contact me.

Department's Response:

In your letter, you state that the "molds and dies purchased are made pursuant to the specifications of Company to fulfill orders from its customers." You clarified this statement during a telephone conversation on January 26, 2001 by indicating that if the molds and dies are purchased for the use of only one customer, the customer pays for the molds and dies. However, if the molds and dies are made to COMPANY's specifications, they can be used to fill orders made by any of its customers. You are requesting a ruling on the latter group of molds and dies, e.g. those made to COMPANY's specifications and used to fill orders from any of its customers.

Section 130.2115, Sellers of Machinery, Tools and Special Order Items, states in part as follows:

a) When Liable For Retailers' Occupation Tax

- 1) Sellers of machinery, tools, dies, jigs, patterns, gauges, models, exhibits, and the like to users or consumers incur Retailers' Occupation Tax liability except as specified in subsection (b) of this Section, and except to the extent that the item sold is exempted by the provisions of the Act. This is true whether the seller installs such tangible personal property for the purchaser or not. (For information concerning the taxability of receipts from installation charges, see Section 130.450 of this Part.)
- 2) The fact that it is not a stock item and is only produced after an order is received, or is an alteration of a standard item, is not sufficient to exempt it from Retailers' Occupation Tax unless it meets all the exemption tests of subsection (b) below.

If the molds and dies are special order purchases pursuant to the provisions of Section 130.2115(b), then Service Occupation and Use Taxes apply. Section 130.2115(b) states, in part, as follows:

b) When Not Liable For Retailers' Occupation Tax

- 1) The seller of a special machine, tool, die, jig, pattern, gauge or other similar item is engaged primarily in a service occupation, rather than in the business of selling tangible personal property, and so does not incur Retailers' Occupation Tax liability with respect to the sale, if the following tests for exemption are all met in the transaction:
 - A) The purchaser employs the seller primarily for his engineering or other scientific skill to design and produce the property on special order for the purchaser and to meet the particular needs of the purchaser;
 - B) the property has use or value only for the specific purpose for which it is produced; and
 - C) the property has use or value only to the purchaser.

If the molds and dies are used to produce products for more than one customer, as in the case you describe for COMPANY, the conditions of Section 130.2115(b) are not met and Retailers' Occupation Tax applies, except to the extent that the item sold is exempted by the provisions of the Act.

Under the Retailers' Occupation Tax Act, the manufacturing machinery and equipment exemption is available for machinery and equipment used primarily (over 50% of the time) in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease. See 86 Ill. Adm. Code 130.330, enclosed. The exemption also extends to repair and replacement parts as long as the parts are incorporated into machinery and equipment that is exempt under the regulation.

"Manufacturing" is defined as the production of any article of tangible personal property, whether such article is a finished product or an article for use in the process of manufacturing or assembling a different article of tangible personal property, by procedures commonly regarded as manufacturing, which changes some existing material or materials into a material with a different use, form, or name. These changes must result from the process in question and be substantial and significant.

Section 130.330(c)(3), which discusses when molds, dies, and jigs qualify for the exemption, states as follows:

Equipment includes an independent device or tool separate from machinery but essential to an integrated manufacturing or assembly process: including computers used primarily in operating exempt machinery and equipment in a computer assisted design, computer assisted manufacturing (CAD/CAM) system; any subunit or assembly comprising a component of any machinery or auxiliary, adjunct, or attachment parts of machinery, such as tools, dies, jigs, fixtures, patterns, and molds; and any parts that require periodic replacement in the course of normal operation; but does not include hand tools, supplies (such as rags, sweeping or cleaning compounds), coolants, lubricants, adhesives, or solvents, items of personal apparel (such as gloves, shoes, glasses, goggles, coveralls, aprons, masks, mask air filters, belts, harnesses, or holsters), coal, fuel oil, electricity, natural gas, artificial gas, steam, refrigerants or water. (Section 2-45 of the Act)

Molds and dies used in a qualifying manner are exempt from Retailers' Occupation Tax as manufacturing machinery and equipment. The molds and dies that you have described are used to manufacture casket hardware. Therefore, they are exempt as manufacturing machinery and equipment.

Please find enclosed a copy of 86 Ill. Adm. Code 130.331 governing the Manufacturer's Purchase Credit. The State of Illinois provides a manufacturer's purchase credit in addition to the exemption for manufacturing machinery and equipment. Purchasers of manufacturing machinery and equipment that qualifies for the manufacturing machinery and equipment exemption earn a credit in an amount equal to a fixed percentage of the tax which would have been incurred under the Use Tax or Service Use Tax. See 35 ILCS 105/3-85; 35 ILCS 110/3-70.

35 ILCS 105/3-85 states, in part, as follows:

"Manufacturer's Purchase Credit. For purchases of machinery and equipment made on and after January 1, 1995, a purchaser of manufacturing machinery and equipment that qualifies for the exemption provided by paragraph (18) of Section 3-5 of this Act earns a credit in an amount equal to a fixed percentage of the tax which would have been incurred under this Act on those purchases. For purchases of graphic arts machinery and equipment made on or after July 1, 1996, a purchaser of graphic arts machinery and equipment that qualifies for the exemption provided by paragraph (6) of Section 3-5 of this Act earns a credit in an amount equal to a fixed percentage of the tax that would have been incurred under this Act on those purchases. The credit earned for purchases of manufacturing machinery and equipment or graphic arts machinery and equipment shall be referred to as the Manufacturer's Purchase Credit. A graphic arts producer is a person engaged in graphic arts production as defined in Section 2-30 of the Retailers' Occupation Tax Act. Beginning July 1, 1996, all references in this Section to manufacturers or manufacturing shall also be deemed to refer to graphic arts producers or graphic arts production.

The amount of credit shall be a percentage of the tax that would have been incurred on the purchase of manufacturing machinery and equipment or graphic arts machinery and equipment if the exemptions provided by paragraph (6) or paragraph (18) of Section 3-5 of this Act had not been applicable. The percentage shall be as follows:

- (1) 15% for purchases made on or before June 30, 1995.
- (2) 25% for purchases made after June 30, 1995, and on or before June 30, 1996.
- (3) 40% for purchases made after June 30, 1996, and on or before June 30, 1997.
- (4) 50% for purchases made on or after July 1, 1997.

* * * * *

In order to calculate the manufacturer's purchase credit on COMPANY's molds and dies, you should calculate tax on 100% of the purchase price of the molds and dies and then divide that amount in half (by 50%).

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.revenue.state.il.us or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

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Associate Counsel

MAJ:msk
Enc.